REMARKS

BY

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SECURITIES AND EXCHANGE COMMISSION

DIRECTORS' COLLEGE, 1999

STANFORD LAW SCHOOL

MARCH 22, 1999
Thank you, Joe, for your generous introduction. I very much appreciate the opportunity to be here this evening. In the last five years, Directors' College has attracted many of this country's most influential thinkers and practitioners in the area of corporate governance.

This year is no different in that respect. But, we gather here tonight during a period in which the broad idea of corporate governance has attracted an unprecedented degree of public attention. One could viably argue that recent high-profile financial reporting failures in corporate America created this attention. Others may point to the increased emphasis placed by the Commission on issues that come under the umbrella of corporate governance.

I don't disagree with those assertions, necessarily. But, more fundamentally, I believe that the increasing imperatives of technologically and globally driven markets are at the source of this greater attention on corporate governance. In the process, more and more people are recognizing that corporate governance is a critical by-product of market discipline.

That's an enlightened and a realistic view. In an age where capital flows worldwide just as quickly as information, a company that does not promote a culture of strong, independent oversight risks its very stability and future health.

For much of modern American corporate history, this evolving consensus was anything but a consensus or even evolving. In 1970, one of the nation's largest companies, Penn Central declared bankruptcy. In the two years before its collapse, the railroad's directors approved dividend payments of more than $100 million while debt soared and working capital deteriorated. The passivity and short-sightedness of Penn Central's board prompted nearly universal criticism.
One article remarked that, "The sad case of Penn Central is worth mentioning not because it is unique, but because it is not. Many another U.S. corporation has gotten into trouble because its directors did not do what they were supposed to do -- that is, keep a warily inquiring eye on management."

Later that year, after conducting hundreds of interviews with corporate executives and directors, a Harvard Business School study concluded that the modern large or medium-sized firms' board of directors had ceased to function as a meaningful check on the corporation's chief executive officer. A senior partner in a consulting group reported in the same study that he didn't know of a single board that really dug into the strategy of the business or held management accountable for results.

But, today, thanks to the swift flow of publicly-disseminated information, corporate decision-making has become more accountable to the true owners of every public company: the shareholders. Over the last two decades, our companies have become more open. Boards are now armed with the information they need to make key decisions and to monitor the performance of corporate managers. Shareholders are now better able to hold corporate directors and officers accountable for their actions.

Why has this happened? Because our capital markets and ultimately, investors demanded it. They want timely, accurate and accessible information. They want responsiveness and they want efficiency. And through the Internet and other new technologies investors have a greater capacity to evaluate those demands more than ever before.

Yet, the same markets that have prompted more and more companies to improve their governance structures and communications with their shareholders have also pushed many other companies to dangerous and ultimately, self-defeating practices.
As many of you know, in recent months I have expressed concern that the motivation to satisfy Wall Street earnings expectations may be overriding common sense business practices. In the process, I fear we are witnessing a gradual, but noticeable erosion in the quality of financial reporting. I'm not the only one. In his annual report released earlier this month, Warren Buffett called the attitude of disrespect toward accurate financial reporting a "business disgrace."

Many of you, I'm sure, are just as frustrated and concerned about this trend as we, at the SEC, are. It's difficult to hold the line on good practices when competitors operate in the gray area between legitimacy and outright fraud.

A gray area where sound accounting practices are perverted; where managers cut corners; and, where earnings reports reflect the desires of management rather than the underlying financial performance of the company. While the problem of earnings management is not new, it has risen in a market unforgiving of companies that miss Wall Street's consensus estimates. For many, this pressure has become all too hard to resist.

As a result, the link between a company's directors and its financial reporting system has never been more crucial. Let me, if I can, take a few moments to discuss this relationship.

Six months ago, I announced a coordinated plan to address the practice of earnings management. Since then, the response from corporate management -- CEOs and CFOs; investors; leaders of the public accounting profession and the halls of academia has been remarkable. I want to commend those in corporate America and the accounting profession for their willingness to step forward and address these insidious practices.

One such effort has been the work of a Blue Ribbon
Committee empaneled to develop recommendations to strengthen the role of audit committees. Sponsored by the New York Stock Exchange and the National Association of Securities Dealers and ably co-chaired by John Whitehead, a former head of Goldman Sachs, and Ira Millstein, a leading corporate governance expert, this group released their report last month.

I'm glad to see you were all given a copy of the report in your materials. This report, bound in an attractive blue and red cover, was not meant to be a handsome addition to your bookshelf. It merits and it demands to be read and re-read.

It is a report that is the product of the leadership of the business community, the accounting profession, the legal profession and Wall Street. As a result, these recommendations are far-ranging, meaningful and relevant to every participant in the financial reporting process.

Suffice to say, I was very much looking forward to the panel's results. I feel passionate about audit committees. For some of you, this might be the first time you have ever heard someone associate passion with a board function.

But, qualified, committed, independent and tough-minded audit committees represent the most reliable guardians of the public interest. Sadly, stories abound of audit committees whose members lack expertise in the basic principles of financial reporting as well as the mandate to ask probing questions. In fact, I've heard of one audit committee that convenes only twice a year before the regular board meeting for 15 minutes and whose duties are limited to listening to a perfunctory presentation.

Compare that situation with the audit committee that meets five times a year before each board meeting; where every member has a financial background; where there are no personal ties to the chairman or to the company; where they have their own advisers; where they ask tough questions of
management and outside auditors; and where, ultimately, the investor interest is being served.

There is no reason why every public company in America shouldn't have an audit committee made up of the right people, doing the right things and asking the right questions.

I believe that the recommendations outlined in the report give companies and auditors the tools they need to make strong and independent audit committees the rule rather than the exception. They are aimed at strengthening the independence of the committee. They seek to make audit committees more effective. They enhance accountability among the board, the outside auditors and management.

And, there are few words more reassuring to investors than accountability. It sends a clear, unambiguous message that you will not sacrifice reputation, stability and long-term growth for short-term vagaries and expectations.

Some, however, have suggested that these recommendations may expose audit committee members to increased liability. As the theory goes, audit committees that write a general description of their responsibilities and have meaningful discussions with management and outside auditors on important financial reporting issues expose themselves to greater liability. If I were an investor, I would find it hard to believe and would be terribly distressed if the law prevented my board from doing just those things.

These aren't academic concerns. What we are talking about goes to the very heart of what audit committees and boards of directors do. And, that is to fulfill a legal duty and a moral mandate to be the shareholder's representative.

So, when the typical refrain on legal liability is invoked, I can't help but wonder if the implicit warning is that boards should be extremely careful what fights they pick or where they should tread. Controlling exposure to
unreasonable litigation risk is clearly an appropriate concern, and I don't want to minimize it. But when it's used unrealistically to thwart board action in the interest of shareholders, it's nothing more than a red herring.

I refuse to believe that more information, more public disclosure, and more active and diligent oversight creates greater legal exposure. I refuse to believe that the clear and necessary delineation of basic responsibilities creates greater legal exposure. I refuse to believe that concern over the quality of financial reporting instead of just merely the acceptability of it creates greater legal exposure. And, I refuse to believe that the vigorous protection of the shareholder interest creates greater legal exposure. These beliefs are not based on a hope of what the law should be, but what most corporate lawyers recognize it actually is.

If Delaware corporate law and the SEC's own administrative actions stand for a single proposition, it is that an active, involved and educated committee or board can rest more easily at night than a board composed of directors who merely go through the motions and watch the clock.

Now, I appreciate that boards face inherent limitations on what they are able to do. I've been a director, and I know what heavy burdens they bear. Directors must review and approve mergers, acquisitions, and combinations that are more complex than ever before. They must answer the demands of institutional investors, who are vocal and vigilant in defending their interests. They must hire and fire managers, and set their compensation based on targets that constantly change.

I can see how, sometimes, the job might feel like it is an impossible one. We should not unfairly second-guess directors -- particularly in the bright light of hindsight -- and make them unreasonably vulnerable.

I also recognize the practical concern of being able to
attract and retain qualified individuals. But, these recommendations won't unduly exacerbate those demands. In fact, they give audit committees the tools to manage and deal with those tasks more pro-actively, more competently, and more effectively.

In specifically proposing that the outside auditors discuss with the board its observations on the quality, not just the acceptability of the financial statements, the Blue Ribbon Panel recognized the systemic importance of justifying decisions that directly affect the quality of a company's financial reporting. When auditors and the board engage in frank and meaningful discussions about the significant, but often gray areas of financial accounting, the ultimate interests of the company and its shareholders are served.

This recommendation is not meant to supplant the board's judgment for that of management's or the outside auditors. But, an effective system exists when the board, including the audit committee, the financial management and outside auditors form a "three-legged stool" to support responsible financial disclosure and active and participatory oversight.

On the plane coming here last night, I began reading over the profiles of the ten outstanding directors for 1998. I was struck by a number of salient and common traits among the group -- above each of their personal accomplishments. First, they were all intimately familiar with their company's operations. Second, they all recognized, in the words of one director, to "strike a balance between short and long-term goals."

Third, they all showed a complete willingness to not only identify problems but also find solutions to them. Fourth, they were all willing to quote "ask the damnedest questions." I especially like that one. And fifth, their dedication and integrity as directors were never questioned.

While these all sound straightforward enough, they are,
by no means, universally performed. We've seen too many examples of companies whose boards could and should have been doing better jobs. There are too many boards that overlook more than they oversee; too many boards that substitute CEO directive for board initiative; too many boards that are re-active instead of pro-active; and too many boards who never rejected an easy answer and never pursued a tough question.

As directors, you may frequently hear the words, duty, obligation and responsibility. After a while, they may sound even a bit trite. But, as directors, those words are your code -- the driving forces behind your mission. And the effects of how you do your job extend far beyond one company's balance sheet.

By safeguarding the value of shareholder interest, you safeguard the integrity of our markets. No regulatory body with all the resources in the world can fully oversee the management of every company. We depend on you. Your supervision complements our oversight. You are in an ideal position to monitor new developments and troubleshoot problems as they arise. The force of your example in leadership far outweighs any authority the SEC might wield.

I ask you to continually assess your priorities as well as management's. I ask you to continually weigh the level of commitment to shareholders. How? Ask yourself as well as management straightforward questions.

For instance, how many times a year does the board meet? If you and your colleagues are meeting a handful of times a year, how can you really expect to exert a strong degree of oversight? American companies today are more competitive than ever. Strategic plans are not only complex, but also more fluid in order to meet the demands of new technology and greater competition. Being an effective corporate director requires time and commitment. It requires involvement and understanding. That doesn't come from one or two meetings a year.
What kind of people are on the board with you, and how did they get there? Too many companies, today, have board members with personal or social ties to the CEO. I'm reminded of the story of a secretary who asked a young man, "How'd you get to be on the board of this company at such a young age?" The man shrugged modestly and explained, "I ran into my father and he took a liking to me."

Do you and your colleagues speak your minds or are you expected to be nothing more than "parsley on fish?" This last phrase was used by an independent director who quit after she felt the company wasn't acting in the best interest of shareholders. I wonder how many companies actively search for directors who won't be outspoken; who go with the flow -- no matter if it's moving in the wrong direction. And, I wonder how many companies try to ease out directors who regularly speak up at meetings in defense of the shareholder; who are willing to break the "code" of silence.

I am disturbed when I read comments such as this one: "By speaking out, directors are virtually guaranteed that they will be blackballed from other boards." Companies that adopt such an attitude are only biding their time before investors decide that their money is better invested elsewhere. In fact, strong, pro-active, and longer-term oriented companies are probably falling over themselves to attract the best corporate directors they can get.

Here are some other questions: do you and your colleagues understand where the company has been and where it is headed? Is there a plan for the future? Is management succession accounted for? Does the board regularly review and evaluate the CEO? Does the board meet at least once a year with the auditor?

These questions are among the first I would ask in evaluating the independence and effectiveness of a board. But they are only the beginning. The marketplace of the
21st century will only create new challenges for America's companies and its board rooms.

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The dynamic nature of today's capital markets creates issues that increasingly move beyond the bright line of right and wrong. More often, financial market participants grapple with questions in a gray area where there are no easy answers. It is in this realm where judgment and integrity are indispensable for effective corporate governance.

These are not easy times. Pressures proliferate. Responsibilities overlap. Objectives run counter to each other. Demands often are at cross-purposes. But, investors, regardless, continue to value companies that achieve value through honesty and hard-work.

Your individual and collective commitment as directors who honor and practice these values is absolutely necessary for long-term health and prosperity - not only for your company - but for our country.

Thank you.